

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF ALABAMA

In re

TERRY MANUFACTURING
COMPANY, INC.

Case No. 03-32063-DHW
Chapter 11

TERRY UNIFORM COMPANY, LLC,

Case No. 03-32213-DHW
Chapter 11

Debtors.

MEMORANDUM OPINION

Cintas Corporation No. 2 filed a motion on April 2, 2004 under 11 U.S.C. § 1112(b) to convert the above-styled chapter 11 cases to cases under chapter 7.

The bankruptcy administrator and chapter 11 trustee of Terry Manufacturing Company, Inc. consent to the motion. The Official Committee of Unsecured Creditors objects to the motion. The committee requests that the cases remain in chapter 11 for liquidation through a confirmed plan to be filed by the committee.

The motion came on for hearing on May 12, 2004. The parties agree that no factual issues are in dispute.

Cintas contends that "cause" exists under 11 U.S.C. § 1112(b) to convert the cases to chapter 7. Cintas points to a "continuing loss to or diminution of the estate and absence of a reasonable likelihood of rehabilitation." 11 U.S.C. § 1112(b)(1). The court agrees.

The arguments on both sides of the issue are a matter of record and will not be reiterated by this order. The court will endeavor to briefly state its reasons for concluding that conversion is in the "best interest of creditors and the estate." 11 U.S.C. § 1112(b).

From the inception of these cases almost one year ago, the trustee and creditors expressed a hope of preserving and selling these businesses as a going concern to maximize the return to creditors. However, over the months their goal has proven impracticable if not impossible. The businesses have ceased operating, and the trustee is engaging in a piecemeal liquidation of the assets of the estates.

Other than the remaining tangible assets, the businesses have avoidance actions which may produce significant returns for the estates. Indeed, their value is estimated in the millions. The ultimate distribution of the assets will be determined by strongly contested litigation regarding the priority and validity of various liens.

Needless to say, the cases are currently in both liquidation and litigation mode. The question arises: which chapter affords the most cost effective manner of completing the administration of these estates?

Chapter 11 requires administrative expenses associated with the confirmation process which are avoided by chapter 7. These include the expense of drafting and noticing a plan and disclosure statement, soliciting and reviewing ballots, and attending hearings and proffering evidence to obtain approval of the disclosure statement and confirmation of the plan. In addition, a committee of unsecured creditors adds another layer of administrative expense to many chapter 11 cases. However, the need for a committee lessens when a case assumes a liquidating posture.¹

¹ A committee serves the very useful purpose of representing the interests of unsecured creditors in the face of a reorganizing debtor. The committee can advise creditors of their rights under a proposed plan and negotiate for better treatment. Committees in chapter 7 are rare because a chapter 7 trustee can usually represent very effectively the interests of unsecured creditors. Indeed, a chapter 7 trustee is charged with the fiduciary duty to maximize the estate for the benefit of unsecured creditors.

The court concludes that the additional administrative expenses inherent in chapter 11 would unreasonably diminish these estates and that conversion is in the best interest of creditors and the estates.

The question becomes: who should be appointed as interim chapter 7 trustee?

The chapter 11 trustee, J. Les Alexander, has indicated a willingness to serve as chapter 7 trustee following conversion. See 11 U.S.C. § 701(a)(1). However, the bankruptcy administrator and Cintas recommend appointment from the panel of trustees serving this district.

J. Les Alexander is a Certified Public Accountant and Managing Principal of AEA Group, LLC. AEA Group is an accounting, economics and appraisal consulting firm specializing in providing advice to companies involved in complex financial challenges and management performance issues. Alexander is also a Certified Fraud Examiner. He resides in an adjacent district.

SouthTrust Bank and First Bank, two of Terry Manufacturing's primary lenders, employed AEA Group, LLC to investigate an unexplained and precipitous \$35 million decline in the company's assets within a few months preceding the chapter 11 petition. The principals of Terry Manufacturing were unwilling to cooperate with the investigation, and the two lenders filed a complaint in state court for the appointment of a receiver to take control of the assets of Terry Manufacturing. Terry Manufacturing then filed the instant chapter 11 case on July 7, 2003.

The lenders immediately sought the appointment of a chapter 11 trustee and recommended Les Alexander. The complexities, peculiarities and exigencies of this case required a trustee with expertise in the specialized field of forensic accounting. The case was filed amid suspicions of fraud and other criminal activity. The security of the assets and records, both documentary and computerized, was at stake. Alexander, through his association with AEA Group, had the knowledge and expertise to

expeditiously assume the role of trustee.

The business records were in shambles and to a large extent, nonexistent. The trustee launched a massive effort to secure and protect the integrity of the remaining records and assets as well as reconstruct the business which operated in three different states. The trustee filed a chapter 11 petition on behalf of Terry Uniform Company, LLC, a wholly owned subsidiary of Terry Manufacturing. The trustee assembled a professional team, including AEA Group and two legal firms, with which he has worked for 10 months to preserve the estates and maximize the return for creditors.

Les Alexander has gained a wealth of knowledge concerning the assets and liabilities of these companies. Some of this knowledge may not be recorded or documented and therefore not immediately accessible or transferrable to a successor trustee.

Given Alexander's knowledge, experience, and expertise, the court is persuaded that Alexander should continue as trustee of the chapter 7 estates absent some compelling or disqualifying reason.

Cintas contends that the relationship between Alexander and AEA Group raises at least the appearance of a conflict of interest. Cintas cites three ways in which that appearance is purportedly manifested.

First, Cintas references AEA Group's prepetition representation of SouthTrust Bank and First Bank. As stated above, the banks employed AEA Group to investigate a decline in the assets of Terry Manufacturing shortly before the petition was filed. However, no objections were filed to Alexander's initial appointment. Nor have any objections to his chapter 11 service been filed to date. SouthTrust Bank and First Bank did not employ Les Alexander individually; they employed the company of which he is the managing principal.

Second, Cintas references AEA Group's postpetition administrative

claim for professional accounting services rendered to the trustee. However, that claim does not give Alexander an interest adverse to the estates. 11 U.S.C. § 327(d) permits a court to authorize a “trustee to act as attorney or accountant for the estate if such authorization is in the best interest of the estate.” Therefore, Alexander could have properly employed himself with court authorization. Certainly he can employ the company of which he is the managing principal.

Third, Cintas references Alexander’s alleged statement that “he does not find the claims asserted by the Committee [against the two banks] to be of merit.” Alexander’s alleged statement refers to an adversary proceeding filed by the committee to determine the extent, validity, and priority of the banks’ liens and to equitably subordinate their liens, if any, under 11 U.S.C. § 510(c).

However, a chapter 7 trustee has the fiduciary duty to investigate any and all claims, including any claims against the two banks. If the trustee determines that the claims have “inconsequential value and benefit to the estate,” the trustee may take the proper steps to abandon the claims under 11 U.S.C. § 544. Fed. R. Bankr. Proc. 6007 requires notice of any proposed abandonment to all creditors. Any party in interest may file an objection. A hearing on any objection is required. Rule 6007(a).

In addition, the trustee does not have exclusive standing to prosecute an action for equitable subordination of a creditor’s claim. *In re Vitreous Steel Products Co.*, 911 F.2d 1223 (7th Cir. 1990). However, even if the trustee has primary standing prosecute such an action, the court may authorize a creditor to proceed if the trustee refuses. *First Bank Billings v. Feterl Mfg. Co. (In re Parker Montana Co.)*, 47 B.R. 419 (D. Mon. 1985).

Therefore, the court finds the reasons asserted by Cintas against Alexander’s appointment to be neither compelling nor disqualifying.

The court is also mindful of the two-year statute of limitations existing under both 11 U.S.C. §§ 108 and 546. While no parties have

argued that the one year remaining under the two-year period is inadequate for a new trustee to become familiar with the claims of the estate, the statute of limitations is another ground in favor of Alexander's appointment. The claims of the estates against other parties are acknowledged to be the major assets of these estates.

For the reasons stated above, the court will enter an order converting these chapter 11 cases to chapter 7 and appointing J. Les Alexander as interim trustee of each estate.

Done this 13 day of May, 2004.

/s/ Dwight H. Williams, Jr.
United States Bankruptcy Judge